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C O N F I D E N T I A L SECTION 01 OF 04 TUNIS 000286

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TAGS: ASCH OFDP PREL TS
SUBJECT: TUNIS AMERICAN SCHOOL NEGOTIATIONS FRUITFUL, BUT
NO DEAL YET

REF: TUNIS 243 AND PREVIOUS

Classified By: Ambassador Robert F. Godec for reasons 1.4 (b) and (d)

Summary

¶1. (C) On May 6-8, US and Tunisian delegations made substantial progress toward resolving the status and financial obligations of the American Cooperative School of Tunis (ACST). The GOT offered formal status for the school and reduced its demand for back taxes from 9.1 to 4.2 million Tunisian dinars with a three-year, zero-interest payment schedule. The GOT also insisted that the school pay new taxes going forward, but made concessions to keep those manageable. ACST has determined that it can accept the new obligations and back tax settlement, although doing so will require an immediate increase in tuition and fees. As a result of the talks, we are close to an agreement, but some issues remain, most importantly the status of ACST's lease. In paragraphs 19-21 we propose next steps and offer our analysis. End summary.

The Delegations

¶2. (U) The Tunisian delegation was led by Ministry of Finance Director General Noureddine Friaa of the National Verification and Fiscal Audits Unit accompanied by Director General Habiba Louati of the Fiscal Legislation Unit, Senior Auditor Maher Janhani and Director of Coordination and Follow up Maher Chikhaoui. Friaa and Janhani had previously led direct talks with ACST that made no headway. The one MFA representative was quite senior in the person of Director of Judicial Affairs Mondher Dhraief (equivalent to the Department's Assistant Secretary for Legal Affairs).

¶3. (U) The US delegation was led by DCM Marc Desjardins joined by Martin Hohe of NEA/SCA/EX, Beatrice Cameron of A/OPR/OS, Clifton Seagroves of DS/OFM/PTSB, Hollin Dickerson of L/DL, Management Counselor Christopher Dye and Information Officer (and ACST Board President) Matthew Long. The negotiations took place at the offices of the Ministry of Finance's National Verification and Fiscal Audits Unit. The GOT provided an appropriate setting and professional simultaneous interpretation to facilitate the talks.

Day 1 - Kabuki Theater

¶4. (C) As the Ambassador had predicted to the delegation, the first day of the negotiations consisted of a four-hour,

painfully exhaustive, point-by-point review of the Tunisian position as already stated in the audit and final tax decree. At appropriate moments, the US side pointed out inconsistencies in GOT arguments, offered alternate interpretations of documents cited and repeated frequently the need for a clear status agreement to place the fiscal issues in context.

¶5. (C) The Tunisian delegation seemed unwilling to bend on the 9.1 million Tunisian dinar sum demanded or even on basic points such as the school's non-profit nature, continuing to classify the school as a for-profit service cooperative. The first day ended with the Tunisian side having obviously exhausted their initial talking points. The US side delivered a strong message that the problem required a focus on a comprehensive solution that acknowledged practical realities.

Day 2 - Real Negotiations Begin

¶6. (SBU) The Tunisian delegation opened the second day of talks with a concrete offer on both past taxes and future status and obligations. In recognition of the school's non-profit nature, the GOT offered exoneration of all corporate and municipal taxes, past and present. On value added tax (VAT), the offer included exoneration from VAT of the school's cafeteria and bus services past and present, forgiveness of penalties but not principal for VAT on past purchases in a spirit of "shared misunderstanding," and a very limited VAT exoneration on future purchase of an

educational nature.

¶7. (SBU) On the other hand, citing the bilateral taxation treaty and "principle," the Tunisian side insisted on all past withholding taxes noted in the audit, and offered a 25 percent flat rate withholding for overseas hire employees in the future. However, overseas hire employees would be granted a "tax holiday" for the 16-month period between the December 31, 2007 end of the audit and the proposed May 1, 2009 implementation date of the new agreement. The total offer on the table was 5.6 million Tunisian dinars with 20 percent down and the rest over three years without interest plus an amount to be determined to settle the local and miscellaneous withholding for the 16-month period.

¶8. (SBU) The US side acknowledged the great progress that had been made since the previous day but insisted on the need for the final solution to be based not only on principle, but on financial reality that would ensure the school's continued fiscal viability. For the future, the Tunisian offer was generally acceptable, the only caveat being a request that the withholding rate on overseas hires be reduced to perhaps 10 percent.

¶9. (C) On the past, the US counteroffer was to pay all the local and miscellaneous withholding due but no overseas hire withholding on the basis of the crucial 1984 diplomatic note that indicated the GOT intention to exonerate school personnel from taxation (an interpretation strongly disputed by the Tunisian side). Also included was half the principal due on past VAT exonerations in a spirit of shared misunderstanding, for a total of 1.5 million Tunisian dinars plus settlement of the local and miscellaneous withholding for the 16-month period.

Land Issues

¶10. (C) The US side raised another issue intimately linked to the school's financial health--a letter from the Ministry of Public Lands to the ACST Board President stating that the

school's current lease (valid until 2025) would be revoked if the school did not agree to renegotiate the very favorable current terms and instead pay commercial rates. Since the school's facilities would revert to the state if the lease were revoked, this represented a serious concern.

¶11. (C) The US delegation insisted that there could be no agreement on taxes and status that did not include, at the very least, guarantees that the lease would not change. An unforeseen change in its terms or its revocation would throw the school into financial chaos, making any status and tax agreement untenable. Indeed, the US delegation suggested that if the GOT were to donate the land to the school, the school would be in a better position to assume the tax obligations demanded since it would have then have the collateral to secure a loan. A donation would also be a fitting recognition of the great economic benefit to Tunisia of the school's presence in attracting diplomatic missions, foreign investment and international organizations.

¶12. (SBU) The GOT did not accept the US proposal but agreed to look into the land issue and indicated that, in principle, the land question could be part of a comprehensive status agreement. Both sides agreed to return the next day for an additional third day of talks. The US side spent the afternoon and evening in consultation with ACST officials and the school's legal and financial advisors crunching numbers, reviewing scenarios and discussing the school's absolute financial red lines.

Day 3 - Brass Tacks

¶13. (C) On the third day of talks, the Tunisian delegation restated their previous offer while correcting an error in calculation to adjust the total to 5.3 million Tunisian dinars plus the 16-months of local and miscellaneous withholding estimated by school officials at approximately 600,000 Tunisian dinars. Indeed, the Tunisian side essentially reviewed at great length the generosity of their previous offers and their magnanimity in not auditing and fining the individual teachers. While noting the need to clarify the lease question, no insight was offered into the resolution of the land issue. The MFA attorney, with a copy

of the Ministry of Public Lands letter in hand, attempted to suggest that the letter was just an invitation for a "friendly discussion" but he did not insist when the US side declined to accept that interpretation.

¶14. (C) In recognition of the Tunisian delegation's clear fixation on withholding taxes above all else, the US side upped its offer to a total of 2.4 million Tunisian dinars calculated to include all local and miscellaneous withholding and half of the withholding on overseas hires in a spirit of shared misunderstanding. That number would, however, be a lump sum payment for all obligations, effectively exonerating all past VAT purchases and including local and miscellaneous withholding in the 16-month tax holiday. The US side also again requested that the future withholding rate on overseas hires be lower. The Tunisian side, after an exhaustive discussion on foreign withholding, rejected that offer.

¶15. (C) After the US side implied that that we seemed to be at an impasse, the Tunisians withdrew for consultations and returned with their "best and final offer." Full exoneration for past VAT would be granted, local and miscellaneous withholding would be included in the tax holiday, and the future withholding rate would be dropped to 20 percent, the same rate offered as an investment incentive to fully-exporting offshore companies. All withholding taxes noted in the audit remained due, however, reducing the one-time settlement amount to 4.2 million Tunisian dinars at 20 percent down and the rest over three years without

interest.

¶16. (C) The Tunisian delegation intimated that more favorable terms might be worked out if the US delegation would commit to the 4.2 millQn Tunisian dinar sum. The US side was unable to accept, however, as the amount was substantially more than the red line previously established with the school and it was unclear whether or not the school could actually honor such terms. The talks ended amicably, with both sides open to future discussions to bridge the gap on this last critical point.

ACST Agrees, Requests Terms

¶17. (SBU) In a May 11 special executive session, the ACST Board of Governors, Director and key administrative personnel were briefed on the status of negotiations and reviewed financial implications of the deal now on the table. ACST agrees that the proposal outlined for the school's future status, while requiring substantial increases in tuition and fees to fund, is not unreasonable and would offer the school clear legal and fiscal status for the future. The proposed 4.2 million Tunisian dinar settlement for past tax liability, while painful in the short term, actually has less impact on the school's overall financial health than the long-term obligations depending on the payment terms.

¶18. (C) In order to secure that future status and in the context of a comprehensive agreement which includes resolution of the land issue, the Board voted unanimously to authorize the US negotiating team to accept the 4.2 million Tunisian dinar GOT offer on two conditions: First, that the payment terms be extended to 10 percent down and the rest over ten years to soften the economic blow to this non-profit institution. Second, that the implementation date and tax holiday be extended by 60 days to July 1, 2009 to allow the school to put into place the procedures to be in compliance and to coincide with the school's July 1-June 30 fiscal year. If the school were granted ownership of the land, however, the GOT offer and terms would be acceptable outright.

Next Steps

¶19. (C) Post believes that the Ambassador should approach the Minister of Finance and the Minister of Foreign Affairs with a non-paper recapping what has been agreed to at the negotiating table, stating that the deal could be closed with the points in paragraph 18 provided that the land issue is unequivocally resolved. The Mission will send a draft non-paper to NEA/MAG for appropriate clearance. Once agreed, we believe it would be useful for the Department to deliver the same paper to Ambassador Mansour in Washington.

Comment

¶20. (C) Despite initial bluster and regardless of any other motivations behind the scenes, the GOT has come a long way from its initial position that the school was a for-profit cooperative with no claim to any special status. On issues such as import/export of personal effects, vehicles or other common benefits, the GOT has cited language already implemented in bilateral agreements with the French and Italian governments. In light of ASCT's willingness to bite the bullet in the short term in exchange for clear status in the long term, and as long as the land issue is resolved and the GOT continues to engage constructively, a bilateral accord seems within reach to ensure ACST's continued service to the community for another 50 years.

¶21. (C) Clearly, the improved outlook for the future of ACST is the result of efforts by many people across the Department. Special thanks go to the Washington-based members of the negotiating team for their efforts and insights and to their offices (NEA/SCA/EX, A/OPR/OS, DS/OFM/PTSB, L/DL) for allowing them to travel to Tunis for the negotiations. Post would also like to thank the NEA Front Office and NEA/MAG for their staunch support throughout this crisis. End comment.
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